

Brokered CDs-A Wolf in Sheep's Clothing?

You've probably seen ads or gotten phone calls or e-mails from brokers saying they've negotiated great deals on federally insured CDs—certificates of deposit—that can mean higher returns than you'd get on your own from a bank. Sounds like a great deal, right? Well, it may or may not be, depending on the offer itself and your personal investment goals.

Generations of Americans have known the CD as a simple, safe, reliable investment for their hard-earned money. With a traditional CD from an FDIC-insured bank or savings institution, if you keep funds in an account for a set period, generally from three months to five years, you get all your money back plus fixed-rate interest payments that are higher than those for regular savings accounts. The guarantees of FDIC insurance, a fixed interest rate, and no loss of principal make the CD especially attractive to consumers who don't want to take chances with their money. Brokers sometimes find or are able to work out special deals on CDs, which enhance the return rate, under certain circumstances, making them appear more attractive than standard CDs.

However, these products can carry hidden or complex features, not easily apparent, which could lead to a less-than-desirable or expected outcome for your investment situation. Here's what this situation can look like: The broker may say that if you need your money before the CD matures, the firm will purchase your CD back *without* an early withdrawal penalty. While this feature may sound attractive, the buy-back offer probably means that the broker would attempt to find someone else to buy your CD at the going market rate. If interest rates on new CDs have increased above the rate your old CD pays, your broker would try to find a buyer by selling your CD at a discount—a loss to you that could be more than a bank's early withdrawal penalty, perhaps even resulting in *a loss of some of your original deposit*.

The bottom line is that before you invest in a CD through a broker, you need to understand the terms and be comfortable that the CD the broker is offering fits your needs. Otherwise, you could find yourself unpleasantly surprised when you realize that the CD you purchased from the broker isn't what you thought it was, based on your past experience buying CDs from your local bank.

Here are some helpful tips that can be implemented when choosing CDs:

3. Make sure your deposit is fully insured.

If full FDIC insurance coverage is important to you—to protect you from loss in the event of a bank failure—we suggest you take these precautions.

Get the name of the bank or savings association where your money is to be deposited. With this information, you can verify that the bank is FDIC-insured. (Call the FDIC's consumer affairs staff or search the FDIC's database of insured institutions at www2.fdic.gov/structur/search/findoneinst.cfm on the Internet.) You'll also learn if the broker plans to put money into an institution where you already own other deposits. This is important to know, because the combination of the brokered CD and your existing deposits could push your total deposited funds over the \$100,000 insurance limit.

Also, insist that the broker give you a copy of the exact title of the CD issued by the FDIC-insured bank or savings association. Why? Because if the CD is to be shared by you and many other customers, the deposit broker probably won't list each name in the CD's title. That's permissible, but you'll still want the account records to somehow indicate that the broker is acting as an agent for you and other depositors (such as "XYZ Brokerage as Custodian for Customers"). That way, *each depositor can qualify for up to \$100,000 of FDIC coverage*. Otherwise, the FDIC would treat the broker as the owner of the CD and insure it only to \$100,000 in total, even if the broker pooled the funds of many different depositors into one CD totaling more than \$100,000. If the broker refuses to provide you with documentation reflecting the title, you should not entrust your money to the broker. The Arizona Securities Division has several publications regarding FDIC-insured products and their features. You can call the Division for free copies of these publications at (602) 542-4242 or toll free at **1-866-VERIFY-9**.

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